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Dairy and Products

Dairy Market Update

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Report Highlights:
Massive dairy farmers' protests have led to a Government decision for increased national domestic support, and to a special request to the EC to exceed the already agreed limits of national subsidies. Dairy industry has faced a serious widening gap between increasing production costs and low milk prices which have accelerated restructuring in the sector, triggered excessive slaughter and resulted in lower milk production. It still remains to be seen if the country will be able to fully utilize the higher milk deliveries quota granted by the EC in late 2007 at Bulgarian request.

Includes PSD Changes: No
Includes Trade Matrix: No
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Summary

Following the disastrous drought in the spring/summer of 2007, the dairy sector has faced the challenge of feedstock deficits, record high input costs and low purchase prices for raw milk combined with negligible domestic support. Dairy farmers have gone out on the streets in the most massive protests ever for more than 3 months, since December 2007 to date.

Protests were nationwide and in some places were supported by grain farmers who were insisting on compensation for spring crop losses. In most cases, producers blocked highways or downtown areas with cattle. Some of them reported that cows could not even walk from malnutrition, and have slowly died. Others claimed that slaughterhouses did not accept cows even for slaughter due to under-standard weight.

Continuous protests and negotiations with the MinAg have not produced the expected results. Farmers blamed the government for lack of strategy, vision, analysis and forecasts for the dairy sector; for its slow reaction, and general reluctance to formulate and follow consistent policy towards the dairy sector. While millions in EU pre-accession funds were spent for subsidized investment in dairy processing factories, almost no EU or domestic support funds have been provided for primary dairy farming.

Farmers requested significant domestic support in the form of a much higher annual subsidy per dairy animal; emergency subsidies for purchase of feed; and increased subsidies for quality milk. They estimated their annual needs at 35-40 million Euro for milk subsidies and 100 million Euro for purchases of feedstock, or total about 140-150 million Euro.

Current situation in the livestock sector

Production cost issue

The MY2007/2008 drought led not only to record high feed grain prices but also to limited production of rough forage and silage. Other input costs such as labor, land rent, veterinary medicine and taxes, fuel, electricity, and farm equipment have increased sharply since the summer of 2007. Most dairy farmers had to borrow to upgrade their farms in order to meet the EU hygiene requirements and be able to apply for dairy quotas. Most recently, the average interest rate on these loans has also risen.

While overall costs for milk (70 percent of which is feedstock) have increased by over 250 percent, the ex-farm prices for raw milk were only 30 percent higher (from 0.25 Euro/liter to currently 0.30-0.36 Euro/liter in various regions). Depressed beef prices (about 1.0 Euro/kilo LWE) also contributed to the crisis.

Average ex-farm price for raw milk in 2007 rose by 17.1 percent to 0.24 Euro/liter. Since June 2007, the average milk ex-farm prices were increasing every month, from 0.20 Euro/liter to reach 0.30 Euro/liter in December 2007. This trend slowed in early 2008 and current prices range from 0.30 to 0.36 Euro/liter as of February 08.

It is estimated that dairy farmers will be profitable if the ratio of milk to feed prices is 1: 2.5 or 1:3; or one liter of milk has to buy 2.5-3.0 kilos of feedstock. During 2007, this ratio was well below the norm since feed prices (wheat, corn and barley) were increasing at much faster rate, and at higher levels compared to milk prices. Thus, the average ratio of milk to corn price for the year 2007 was 1.3; milk to wheat was 1.4 and milk to barley was 1.5, or a liter of milk was sufficient for purchases of less than 1.5 kilos of any feed. In early 2008, this index declined further with the new record high feed prices and stagnating raw milk prices.

Feed deficit issues made merging, acquisitions and enlargement of farms faster but also much more painful. For example, the number of the first category dairy farms (see BU7023), which fully meet EU criteria (853/2004/EC) have increased from 993 as of January 1, 2007 to 1,562 as of January 1, 2008 (growth of 57 percent), and the number of dairy cows grew from 44,654 to 63,680 (43 percent). The number of farms in the second group increased as well from 1,095 to 1,196 for the same period, but the cows bred on them dropped from 26,553 to 21,392.

Dairy herd changes

The situation has been especially disastrous at small and medium size dairy farms. Many of those farms were not able to get individual dairy quotas which further contributed to their losses. Larger dairy farms, although less affected by the drought, have reported that the revenue was just sufficient to pay for the production costs with zero profit margins, thus no expansion or growth is likely to occur at these farms in the near future. As a result, excessive dairy cattle slaughtering which began in September became a serious problem in the winter months.

As of the end of February, a MinAg urgent update announced 6 percent reduction in the dairy herd on an annual basis. Some MinAg sources indicated that as of the end of 2007, the number of dairy cattle had dropped to 340,000 cows; 5,000 bufallo; 1,260,000 ewes and 400,000 she-goats. However, industry estimates varied from 5 percent to 15 percent or higher reduction in dairy livestock numbers. As of February 2008, about 3,000 farms officially declared to the MinAg that they closed their business.

Milk production

The MinAg sources expected that problems with feeding and reduced number of animals would lead to lower milk production in 2007. In the period November 1, 2006- April 30, 2007, milk production was 690,000 MT or 6 percent lower than in the previous year. The early annual 2007 estimate was for total milk at 1,461,000 MT (compared to 1,471,000 MT in 2006) of which 1,267,000 cow milk (1,260,000 MT in 2006), 6,000 MT buffalo milk, 101,000 MT sheep milk and 87,000 MT goat milk. These figures, however, were criticized by the industry as too optimistic. The trade speculated that 2007 milk production was much lower, at least 5 percent down from 2006 due to declining livestock; and further negative growth was likely for 2008 vs. 2007.

Milk quotas and regulations

In October 2007, Bulgaria was granted an increase in the milk quota (1186/2007/EC) from 722,000 MT to 889,000 MT for milk deliveries; and 90,000 MT for direct sales, reduced from 257,000 MT. The additional 167,000 MT of milk which were transferred from direct sales to deliveries, was allocated to the milk reserve.

This decision was very important for the dairy industry which back in January 2007 applied for 941,998 MT of milk deliveries or 30 percent above the allowed quota. As a result, the applications, especially of farms in the third category (see various farm categories in BU7023) were cut by 47 percent. This was another reason for excessive slaughter at these farms.

The additional quotas were distributed in January 2008. Total 81,000 farmers received increased quotas. Upon this secondary quota distribution, the applications were still cut but by 20 percent, compared to the initial reduction of 47 percent in April 2007. Another 87,000

MT for deliveries and 2,300 MT for direct sales from the national milk reserve (92,400 MT) were also allocated to farmers.

With the 2 percent annual increase in April 2008, the national quota will be 998,580 MT. Although higher, this amount is still below the demand and the capacity of local dairy processors, 1.2-1.4 million MT.

In December 2007, the MinAg approved a far-reaching regulation for the management of dairy quotas (Decree #23 of December 13, 2007) which canceled the previous regulation (Decree #51 of April 20, 2007). It introduced basic rules for management of the milk reserve; public register of cow milk purchasers/buyers; rules for distribution, transfer and conversion of milk quotas; procedures for approval of milk purchasers/buyers and required bank guarantees; and major rules for overall management of milk purchasing process. The fines were set at 0.28 Euro/liter for milk produced above the quota. The Paying Agency was in charge of execution of controls and had to inspect at least 2 percent of milk producers with milk deliveries quotas, 40 percent of the delivered milk, and 5 percent of producers with direct sales quotas.

The dairy quota as of January 1, 2008 was distributed as follows:

First category farms – total 246,242 MT of which 236,875 MT for milk deliveries and 9,367 MT for direct sales. The MinAg plans that the milk produced at these farms should be 300,000 MT by March 31, 2008 (30 percent of all milk) and about 100 percent of the market by the end of 2009 when the grace period ends.

Second category farms – total 69,719 MT of which 64,719 MT for deliveries and 4,763 MT for direct sales.

Out of total 96,572 dairy producers/farms with milk quotas, 19,429 have individual quotas for both deliveries and direct sales. The average size of the quota is 7,239 kilos for deliveries (87,039 farms) and 1,462 kilos for direct sales (48,391 farms). See Table 2.

As of this writing, a MinAg source indicated that 882,000 MT were distributed for deliveries and 67,000 MT for direct sale, or total 949,000. The remaining quantity of 30,000 MT of the total milk quota (979,000 MT) was allocated as a reserve to be provided to newly established farms and new investment projects under the EU- subsidized investment programs later in 2008.

It remains to be seen if the lower milk production and problems with quota distribution will lead to underutilization of the Bulgarian quota for the first quota year 2007/2008. Currently, FAS/Sofia estimated that the national milk quota will be used at about 90-92 percent.

Dairy products market

Local market

According to industry sources, 20-40 percent higher prices for dairy products have led to more than 25 percent decline in sales of dairy products since the fall of 2007. In addition, a food safety issue in early 2008 negatively affected consumer confidence. In February, Bulgarian consumers witnessed the first ever scandal with listeriosis. Infected milk was sold to nurseries, schools, retail outlets and hospitals in South-West Bulgaria and caused concerns among children and parents. The milk was recalled but the authorities were blamed for slow and delayed action.

In contrast, the cheese market has developed very dynamically, especially the high-end segment. Various trade sources estimated the imported cheese market at 15 million Euro. The usual suppliers were France, Italy, Germany, Holland, Denmark, Spain, Austria. Currently, the cheese assortment on the market reaches over 100 types in an annual volume of 3,500-5,000 MT. Industry estimated the share of imported cheese vs. locally produced at 25-30 percent with a clear trend of growth in both tonnage and value. One major retail chain reported 500 percent growth in sales of imported cheese in 2007 compared to 2002. Cheeses in greatest demand were the “blue” types (about 30 percent share in the imported cheese). Loyal consumers of imported brand cheeses, however, were 12-15 percent of all consumers, and only in urban areas.

Trade

In the period January-October 2007, Bulgaria imported 25,271 MT of milk and dairy products, of which the largest share belonged to whey (7,000 MT) and cheese (3,400 MT). Thus, imports for this period were 37.7 percent more than the same period in 2006. It is assumed that the decline in milk output in the last quarter of 2007 further increased dairy imports. Imports from third countries for the period were 14 percent or 3,471 MT, with the remaining 86 percent (21,800 MT) imported from the EU member states (see Table 1).

The forecast for 2008 is for continued demand for milk substitutes such as milk powder and whey due to lower local milk output; and stable imports of high-end cheeses.

Exports of dairy products in the first 10 months of 2007 were 19,083 MT of which cheese and curd accounted for 13,226 MT or 70 percent. The trend was clearly in favor of higher exports, 49.3 percent more than in the same period a year before. Annual 2007 exports were estimated to be significantly higher than in 2006. About 68 percent of exported dairy products were traded in the EU (12,985 MT) and the rest 6,098 MT were destined for the third markets. In 2008, exports may be restrained by the lack of raw material and shrinking margins due to increased costs; in addition, exports to U.S. dollar destinations (USA, Canada, Australia, Syria and Lebanon) may be limited by the weak dollar.

Government policy

The GOB does not have a history of substantial support for the dairy sector. Over the last several years, dairy farmers were eligible for subsidies for quality milk per liter in the summer season; for some support for breeding stocks; and for subsidized EU-SAPARD investment programs. Since most dairy farms are of small/medium size, many do not have sufficient land and the major SAPS mechanism does not provide enough funds for them. Thus, livestock farmers remain disadvantaged compared to crop growers.

Under the pressure of dairy farmers’ protests, in early 2008 the MinAg expanded its support programs:

- A government decision for an annual (not seasonal/summer as before) subsidy per liter of quality milk was approved for 2008. The allocation for this program was 12 million Euro (this amount included also dairy breeding livestock subsidies). The MinAg began to receive applications in February and to pay retroactively for January. The milk subsidies were increased from 0.04 to 0.10 Euro/liter for cows and goat milk; from 0.035 Euro to 0.125 Euro/liter for sheep and buffalo milk.

Note: In 2007 (as of October 07) quality milk subsidies were paid to about 10,000 farmers at a value of 2.1 million Euro.

- The implementation of the regulation 1535/2007/EC "de minimis" which allows farmers to apply for an emergency subsidy/aid once in 3 years at an amount up to 7,500 Euro/farm, was accelerated. Total allocation under this mechanism was 10.5 million Euro. The MinAg opened the application process in February. It is expected that 90 percent of applicants would be approved for an aid of 4,500 Euro. All aid can be fully paid by May 30. Under this regulation, farmers will be able to receive 150 Euro/dairy cow, 160 Euro/female buffalo, 20 Euro/ewe, and 10 Euro/ she-goat. According to industry sources, this program can cover not more than 27,000 cattle which meet the eligibility criteria.

The above programs in the amount of 22.5 million Euro represent the total financial resources to be allocated under the 2008 national domestic support scheme, or only 15 percent of what farmers consider as an emergency package. If spent in the first months of 2008, no funds will remain for any support later in the year, both for crop and livestock farmers.

For this reason, the MinAg sent a special request to Brussels/DGAgri which called for a permit for additional national domestic support for dairy farmers under various mechanisms. The request was based on the fact that the national domestic support for the dairy sector has been already fixed for 2008. Per the Accession Treaty, it could not be increased by more than 20 percent on the top of the amount paid to farmers in the accession year 2007. If not permitted by the EC, any additional funds for domestic support would lead to a fine by EC. Reportedly, the MinAg has requested permission to spend additional 30-35 million Euro for the dairy sector in 2008 - an amount which is needed only for the milk subsidies. In the request, the MinAg estimated the losses generated by the dairy sector at 136 million Euro, and expected that at least 2-3 years will be needed for the sector to revive. To date, EC has not responded yet to this request.

Table 1. Trade in dairy products (MT) in 2007

Imports of dairy products, MT			Exports of dairy products, MT		
	2006	Jan-Oct.2007		2006	Jan-Oct.2007
Total	20,902	25,271	Total	15,854	19,083
Milk and cream, not concentrated	294	3,742	Milk and cream, not concentrated	316	375
Milk and cream, concentrated	8,183	9,135	Milk and cream, concentrated	79	892
Yogurt	167	608	Yogurt	1,100	3,840
Whey	7,299	7,057	Whey	4	30
Butter and oils	1,361	1,324	Butter and oils	570	720
Cheese and curd	3,598	3,405	Cheese and curd	13,784	13,226
Source: Dairy Situation and Outlook Bulletin, MinAg, February 2008					

Table 2. Dairy farms and milk quotas development, January 1, 2007- February 18, 2008

Time Period	First category farms				Second category farms			
	Number of farms	Number of cows	Milk quotas		Number of farms	Number of cows	Milk quotas	
			Deliveries	Direct sales			Deliveries	Direct sales
Jan 1, 2007	993	44,654	156,170		1,095	26,553	74,361	
April 1, 2007	1,125	46,541	192,432	10,214	1,238	29,393	94,636	6,177
Oct. 1, 2007	1,402	59,064	226,355	10,218	1,235	23,293	70,073	5,825
Jan. 1, 2008	1,562	63,680	236,875	9,367	1,196	21,392	64,719	4,763
Feb.18, 2008	1,583	76,287	317,580	8,385	1,144	22,100	65,640	4,589
Source: unofficial MinAg data								